

**Audited Financial Statements,
Supplementary Information,
and Compliance Reports**

Carolina Small Business Development Fund

Years Ended June 30, 2019 and 2018

Audited Financial Statements, Supplementary Information, and Compliance Reports

Carolina Small Business Development Fund

Years Ended June 30, 2019 and 2018

Audited Financial Statements

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Independent Auditors' Report

Board of Directors
Carolina Small Business Development Fund
Raleigh, North Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of Carolina Small Business Development Fund (a nonprofit organization), which comprise the statements of financial position as of June 30, 2019 and 2018, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Carolina Small Business Development Fund as of June 30, 2019 and 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Adoption of New Accounting Standard

As discussed in note A to the financial statements, Carolina Small Business Development Fund adopted FASB Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

Independent Auditors' Report--Continued

Other Matters

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of federal and state awards, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 30, 2020, on our consideration of Carolina Small Business Development Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Carolina Small Business Development Fund's internal control over financial reporting and compliance.

Romeo, Wiggits & Company, L.L.P.

Raleigh, North Carolina
June 30, 2020

Statements of Financial Position

Carolina Small Business Development Fund

June 30, 2019 and 2018

	<u>2019</u>	<u>2018</u>
ASSETS		
OPERATING FUNDS:		
General deposits	\$ 1,758,495	\$ 1,457,425
Operating deposits	<u>415,643</u>	<u>1,607,104</u>
Total operating funds (cash and cash equivalents)	2,174,138	3,064,529
COMMITTED LOAN SUPPORT FUNDS:		
Small business lending	7,975,281	5,958,165
OTHER COMMITTED SUPPORT FUNDS:		
SEDA - for CDCU lending	160,200	171,262
Mortgage loans - GCCU	<u>136,265</u>	<u>140,428</u>
	296,465	311,690
Less: Reserve on at-risk deposits/mortgage loans	<u>(50,000)</u>	<u>(50,000)</u>
Total other committed support funds	246,465	261,690
LOANS RECEIVABLE:		
Loans - small business lending	29,307,834	30,209,030
Less: Loan loss reserves	<u>(2,054,576)</u>	<u>(2,404,592)</u>
Total loans receivable	27,253,258	27,804,438
OTHER RECEIVABLES		
Grants receivable	688,145	688,178
NMTC Leverage Loan	2,135,000	-
Other	<u>74,441</u>	<u>72,695</u>
Total other receivables	2,897,586	760,873
PREPAID EXPENSES	55,348	72,943
FIXED ASSETS:		
Leasehold improvements	3,508	3,508
Equipment and computers	211,176	205,194
Furniture and fixtures	<u>81,859</u>	<u>81,859</u>
	296,543	290,561
Less: Allowance for depreciation	<u>(254,092)</u>	<u>(206,082)</u>
Total fixed assets	42,451	84,479
TOTAL ASSETS	<u>\$ 40,644,527</u>	<u>\$ 38,007,117</u>
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts payable and accrued expenses	\$ 157,868	\$ 104,937
Accrued vacation	103,820	94,318
Deferred support	31,265	-
Notes payable	<u>25,583,241</u>	<u>23,855,492</u>
TOTAL LIABILITIES	25,876,194	24,054,747
NET ASSETS		
Without donor restrictions	10,059,114	11,311,969
With donor restrictions	<u>4,709,219</u>	<u>2,640,401</u>
TOTAL NET ASSETS	14,768,333	13,952,370
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 40,644,527</u>	<u>\$ 38,007,117</u>

See independent auditors' report and notes to financial statements.

Statement of Activities

Carolina Small Business Development Fund

Year Ended June 30, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
SUPPORT, REVENUES, AND OTHER INCOME:			
Grant income	\$ 3,241,728	\$ 3,287,095	\$ 6,528,823
Contributions	6,947		6,947
Special events revenue	162,983		162,983
Dividend income	45,005	120	45,125
Mortgage interest	8,869		8,869
Loan closing/servicing revenue	78,731	2,851	81,582
Premium on sale of SBA CA guarantee loans	96,561		96,561
Repayment of bad debt	34,002		34,002
Business loan interest	1,770,453	198,932	1,969,385
Origination fees	100,105	7,390	107,495
Membership fees	5,000		5,000
Other income	2,198		2,198
Net assets released from restrictions due to satisfaction of:			
Purpose restrictions	1,355,605	(1,355,605)	-
Time restrictions	71,965	(71,965)	-
	<u>6,980,152</u>	<u>2,068,818</u>	<u>9,048,970</u>
TOTAL SUPPORT, REVENUES, AND OTHER INCOME			
EXPENSES:			
Program services	6,778,650		6,778,650
Support services:			
Management and general	1,374,780		1,374,780
Fundraising	79,577		79,577
Total support services	<u>1,454,357</u>		<u>1,454,357</u>
	<u>8,233,007</u>	<u>-</u>	<u>8,233,007</u>
TOTAL EXPENSES			
	<u>(1,252,855)</u>	<u>2,068,818</u>	<u>815,963</u>
CHANGE IN NET ASSETS			
Net assets, beginning of year	<u>11,311,969</u>	<u>2,640,401</u>	<u>13,952,370</u>
	<u>\$ 10,059,114</u>	<u>\$ 4,709,219</u>	<u>\$ 14,768,333</u>
NET ASSETS, END OF YEAR			

See independent auditors' report and notes to financial statements.

Statement of Activities

Carolina Small Business Development Fund

Year Ended June 30, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
SUPPORT, REVENUES, AND OTHER INCOME:			
Grant income	\$ 2,581,510	\$ 2,067,391	\$ 4,648,901
Contributions	12,617		12,617
Special events revenue	154,672		154,672
Dividend income	35,891	95	35,986
Mortgage interest	7,172		7,172
Loan closing/servicing revenue	85,131	8,583	93,714
Repayment of bad debt	50,861		50,861
Business loan interest	1,594,075	152,832	1,746,907
Origination fees	123,772	5,260	129,032
Membership fees	8,500		8,500
Other income	7,059		7,059
Net assets released from restrictions due to satisfaction of:			
Purpose restrictions	2,122,134	(2,122,134)	-
Time restrictions	70,000	(70,000)	-
	<u>6,853,394</u>	<u>42,027</u>	<u>6,895,421</u>
TOTAL SUPPORT, REVENUES, AND OTHER INCOME			
EXPENSES:			
Program services	5,808,391		5,808,391
Support services:			
Management and general	1,239,764		1,239,764
Fundraising	60,049		60,049
Total support services	<u>1,299,813</u>		<u>1,299,813</u>
	<u>7,108,204</u>	<u>-</u>	<u>7,108,204</u>
TOTAL EXPENSES			
	<u>7,108,204</u>	<u>-</u>	<u>7,108,204</u>
CHANGE IN NET ASSETS			
	(254,810)	42,027	(212,783)
Net assets, beginning of year	<u>11,566,779</u>	<u>2,598,374</u>	<u>14,165,153</u>
NET ASSETS, END OF YEAR	<u>\$ 11,311,969</u>	<u>\$ 2,640,401</u>	<u>\$ 13,952,370</u>

See independent auditors' report and notes to financial statements.

Statement of Functional Expenses

Carolina Small Business Development Fund

Year Ended June 30, 2019

	Program Services	Support Services	Total
	<u> </u>	<u> </u>	<u> </u>
PERSONNEL:			
Salaries	\$ 2,016,618	\$ 590,155	\$ 2,606,773
Employee benefits	270,914	80,923	351,837
Payroll taxes	157,621	47,081	204,702
Total personnel	<u>2,445,153</u>	<u>718,159</u>	<u>3,163,312</u>
OTHER EXPENSES:			
Interest expense	865,018		865,018
Marketing and newsletter	28,742	8,108	36,850
Bank fees	20,214		20,214
Telephone	57,742	16,284	74,026
Professional fees	112,789	31,812	144,601
Contract services	559,242	354,535	913,777
Subscriptions, sponsorships and dues	47,017	13,265	60,282
Staff travel	157,655	44,465	202,120
Seminars, conferences, and workshops	59,191	10,446	69,637
Board meeting expenses	4,992	2,349	7,341
Office supplies and expenses	28,861	7,671	36,532
Printing and copying	10,287	2,901	13,188
Software	76,568	16,145	92,713
Office occupancy	163,870	46,220	210,090
Insurance and bonding	30,753	8,676	39,429
Postage	8,742	2,466	11,208
Provision for losses on loans	1,643,959		1,643,959
Loan servicing fees	140,976	39,762	180,738
Legal expenses	96,406	27,193	123,599
Staff development	48,781	13,760	62,541
Fundraising expense		79,577	79,577
Grant repayment	134,245		134,245
Total other expenses	<u>4,296,050</u>	<u>725,635</u>	<u>5,021,685</u>
Total operating expenses before depreciation	6,741,203	1,443,794	8,184,997
Depreciation	<u>37,447</u>	<u>10,563</u>	<u>48,010</u>
TOTAL EXPENSES	<u>\$ 6,778,650</u>	<u>\$ 1,454,357</u>	<u>\$ 8,233,007</u>

See independent auditors' report and notes to financial statements.

Statement of Functional Expenses

Carolina Small Business Development Fund

Year Ended June 30, 2018

	Program Services	Support Services	Total
PERSONNEL:			
Salaries	\$ 2,044,769	\$ 576,730	\$ 2,621,499
Employee benefits	303,418	85,580	388,998
Payroll taxes	166,170	46,866	213,036
Total personnel	<u>2,514,357</u>	<u>709,176</u>	<u>3,223,533</u>
OTHER EXPENSES:			
Interest expense	594,090		594,090
Marketing and newsletter	54,650	15,416	70,066
Bank fees	19,027		19,027
Telephone	57,843	16,313	74,156
Professional fees	69,353	28,922	98,275
Contract services	828,163	224,228	1,052,391
Subscriptions, sponsorships and dues	87,628	24,723	112,351
Staff travel	178,145	50,244	228,389
Seminars, conferences, and workshops	53,732	9,263	62,995
Board meeting expenses	18,720	8,847	27,567
Office supplies and expenses	45,557	12,343	57,900
Printing and copying	13,134	3,704	16,838
Software	38,916	10,963	49,879
Office occupancy	159,406	45,317	204,723
Insurance and bonding	13,590	3,834	17,424
Postage	8,527	2,405	10,932
Provision for losses on loans	710,884		710,884
Loan servicing fees	41,911	11,818	53,729
Legal expenses	140,325	39,581	179,906
Staff development	40,517	11,428	51,945
Fundraising expense		60,049	60,049
Grant repayment	80,000		80,000
Miscellaneous expenses	75		75
Total other expenses	<u>3,254,193</u>	<u>579,398</u>	<u>3,833,591</u>
Total operating expenses before depreciation	5,768,550	1,288,574	7,057,124
Depreciation	<u>39,841</u>	<u>11,239</u>	<u>51,080</u>
TOTAL EXPENSES	<u>\$ 5,808,391</u>	<u>\$ 1,299,813</u>	<u>\$ 7,108,204</u>

See independent auditors' report and notes to financial statements.

Statements of Cash Flows

Carolina Small Business Development Fund

Years Ended June 30, 2019 and 2018

	<u>2019</u>	<u>2018</u>
OPERATING ACTIVITIES		
Change in net assets	\$ 815,963	\$ (212,783)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	48,010	51,080
Provision for losses on loans	1,643,959	710,884
Interest expense added to borrowings	9,745	15,011
Changes in operating assets and liabilities:		
Grants receivable	33	470,387
Other receivables	(1,746)	(17,547)
Prepaid expenses	17,595	(23,652)
Deferred support	31,265	-
Accounts payable and accrued expenses	62,433	90,691
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>2,627,257</u>	<u>1,084,071</u>
INVESTING ACTIVITIES		
Decrease (increase) in committed loan support funds	(2,017,116)	429,361
Decrease in other committed support funds, net provision for losses	15,225	12,035
Small business loans funded	(8,139,734)	(11,069,149)
Principal payments received on small business loans	7,046,955	4,366,579
Funding of NMTC Leverage Loan	(2,135,000)	-
Purchases of fixed assets	(5,982)	(23,092)
NET CASH USED IN INVESTING ACTIVITIES	<u>(5,235,652)</u>	<u>(6,284,266)</u>
FINANCING ACTIVITIES		
Proceeds from new borrowings	3,575,000	5,834,000
Principal payments on borrowings	(1,856,996)	(705,428)
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>1,718,004</u>	<u>5,128,572</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(890,391)	(71,623)
Cash and cash equivalents (operating funds), beginning of year	<u>3,064,529</u>	<u>3,136,152</u>
CASH AND CASH EQUIVALENTS (OPERATING FUNDS), END OF YEAR	<u>\$ 2,174,138</u>	<u>\$ 3,064,529</u>
SUPPLEMENTAL CASH FLOW INFORMATION		
Interest paid	\$ 772,595	\$ 579,079
NONCASH INVESTING AND FINANCING ACTIVITIES		
Charge-offs against loan loss reserves:		
Uncollectible loans	\$ 1,994,025	\$ 549,140
Withdrawal from mortgage escrow account	-	46,888

See independent auditors' report and notes to financial statements.

Notes to Financial Statements

Carolina Small Business Development Fund

Years Ended June 30, 2019 and 2018

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Organization: Carolina Small Business Development Fund (the Organization/Carolina Small Business/previously known as The Support Center) is a statewide nonprofit and certified Community Development Financial Institution. The Organization’s mission is to foster economic development in underserved communities by providing capital, business services, and policy research to support small businesses.

In 2010, Carolina Small Business launched its Small Business Revolving Loan Fund Program (SBRLF), targeting underserved communities and populations that find it difficult to access capital. The Organization also provides financial training and technical assistance to start-ups and existing businesses and lending services to community-based organizations.

Carolina Small Business is the sole member of Carolina Capital Impact, Inc., a 501(c)3 nonprofit entity formed in March 2017. The subsidiary has no holdings and no activity to date.

Basis of Accounting: The accompanying financial statements are presented on the accrual basis of accounting.

Adoption of New Accounting Standard: The accompanying financial statements have been prepared in accordance with FASB Accounting Standards Update (ASU) 2016-14, Not-for-Profit Entities (Topic 958) - *Presentation of Financial Statements of Not-for-Profit Entities*, which was first effective for fiscal years beginning after December 15, 2017. The Organization is thereby required to report information regarding its financial position and activities according to the following net asset classes:

Net Assets Without Donor Restrictions (including a subsequent event): These net assets are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Organization. The Organization’s net assets without donor restrictions include Board-designated net assets as detailed below. Board-designated net assets are not available to cover operating expenses, including budget shortfalls, unless specifically approved by the Board. Net assets without donor restrictions consist of the following at June 30:

	<u>2019</u>	<u>2018</u>
Operating reserves	\$ 3,101,367	\$ 3,205,802
Board-designated:		
Contingency reserve*	-	1,104,585
Small business lending	6,668,831	6,655,413
At-risk deposits/mortgage loans	246,465	261,690
Property and equipment, net	<u>42,451</u>	<u>84,479</u>
Total net assets without donor restrictions	<u>\$ 10,059,114</u>	<u>\$ 11,311,969</u>

* The Board voted subsequently to remove its designation on net assets held in the Organization’s contingency reserve. The Board also agreed to discontinue the transfer of \$150,000 annually to the Board-designated reserve. The resolution was adopted on January 10, 2020, and was retroactive to June 30, 2019. Net assets of \$1,104,585, held previously in the contingency reserve, are included in operating reserves at June 30, 2019.

Net Assets With Donor Restrictions: These net assets are subject to restrictions imposed by donors and grantors. Some restrictions are temporary in nature, such as those that are restricted by a donor for use for a particular purpose or in a particular future period. Other restrictions may be perpetual in nature; such as those that require resources to be maintained in perpetuity. When a donor’s restriction is satisfied, either by using the resources in the manner specified by the donor or by the passage of time, net assets are reclassified from net assets with donor restrictions to net assets without donor restrictions. At June 30, 2019 and 2018, the Organization has no net assets with donor restrictions that require resources to be maintained in perpetuity.

The Organization has implemented ASU 2016-14 retrospectively for all periods presented. Expenses are reported by nature and function in the statements of functional expenses, and quantitative and qualitative disclosures with regard to the availability and liquidity of assets are described in Note B herein.

Carolina Small Business Development Fund

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -- Continued

Promises to Give: Unconditional promises to give are recognized as support or gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

Recognition of Support: Contributions that are restricted by the donor are reported as increases in net assets without donor restrictions if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the support is recognized. All other donor-restricted contributions are reported as increases in net assets with donor restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as net assets released from restrictions. Unconditional promises to give are recognized as support or gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give (including reimbursement grants) are recognized when the conditions on which they depend are substantially met. Support from loan assistance programs is generally recognized upon closing of the funded loans or upon incurrence of other qualifying expenditures. State awards of \$2,500,000 were fully expended (or committed) and were recorded directly to support without donor restrictions for each of the years ended June 30, 2019 and 2018.

Cash Equivalents: The Organization considers its *operating funds* to be cash equivalents. Operating funds at June 30, 2019 and 2018 consist of amounts held in bank (credit union) checking (savings/master share) accounts, as well as certificates of deposit (share term certificates) with minimal penalties for early withdrawal. Refer also to *Note C--Significant Concentrations*.

Committed Loan Support Funds: Committed loan support funds are available for small business lending, and may be subject to certain restrictions of the donor or creditor agency. These funds are largely held in bank (credit union) checking accounts with various banks, but also include deposits in money market and master share accounts. Refer also to *Note C--Significant Concentrations*.

Other Committed Support Funds: Other committed support funds include SEDA deposits held in a share term certificate and amounts due under mortgages purchased from Generations Community Credit Union (now, part of Self-Help Credit Union). The share term certificate is carried at face value plus accrued earnings thereon. Other committed support funds are recorded net of an allowance for losses on at-risk funds. Refer also to *Note C--Significant Concentrations*.

Loans Receivable: Carolina Small Business originates, processes, and underwrites loan applications and funds, and holds and services small business loans in portfolio. Terms and rates of loans vary depending upon the borrower's capital requirements and management's assessment of risk. Loans are placed on non-accrual status if 90 days past due and not in the process of collection. Loans are secured by the borrower; however, the realizable value of the borrower's collateral is generally dependent upon the operating results of the borrower's small business. Loans may also be secured under guaranteed loan programs and may be sold in the secondary market. Refer also to *Note D--Loans Receivable/Loan Loss Reserves*.

NMTC Leverage Loan: On August 1, 2018, Carolina Small Business agreed to participate as an Intermediary Community Development Entity (CDE) in a collaborative effort to increase investment in low-income communities, while providing investors access to certain New Market Tax Credits (NMTC) allocated by the U.S. Department of the Treasury's Community Development Financial Institutions Fund (CDFI). Carolina Small Business extended a Leverage Loan of \$2,135,000 to a member of the investment group. The Leverage Loan (receivable) requires quarterly interest payments at 5% per annum, with principal due upon maturity on October 31, 2025. The Leverage Loan is collateralized by the borrower's interest in an investee of the investment group, as defined by agreement. Carolina Small Business also entered into promissory notes totaling \$3,050,000 with members of the investment group. The notes payable of \$3,050,000 require quarterly interest payments at 3.5%, with principal due upon maturity on October 31, 2025. Carolina Small Business, in turn, committed loans of \$1,350,000 and \$1,700,000 to two businesses serving low-income communities. For its participation as an Intermediary CDE, Carolina Small Business is designated to receive exit fees of \$205,875, unless otherwise defined by agreement, on or about October 31, 2025.

Carolina Small Business Development Fund

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -- Continued

Loan Loss Reserves: Carolina Small Business provides a provision for losses on loans sufficient to cover estimated credit losses inherent in the loan portfolio, as well as a provision for losses on loans identified as impaired. Funded loan loss reserves are also maintained in compliance with specific funding or program guidelines.

Management utilizes historical losses and loss migration in estimating credit losses in the performing loan portfolio. Historical losses are adjusted for any qualitative or environmental factors that may cause estimated losses to differ from historical loss experience. Non-performing loans are individually evaluated for impairment and specific reserves allocated to cover any estimated impairment. Refer also to *Note D--Loans Receivable/Loan Loss Reserves*.

Grants Receivable: Grants receivable at June 30, 2019, consists primarily of amounts due from federal and state agencies and financial institutions. The Organization has provided no provision for uncollectible accounts since management believes all amounts are collectible. Receivables are unsecured and are expected to be collected within a year.

Fixed Assets: Fixed assets are recorded at cost at the date of purchase or at fair market value at the date of donation. In the absence of donor stipulations regarding how long the contributed assets must be used, contributions of fixed assets are recorded as without donor restrictions. Depreciation is computed over the estimated useful lives of the respective assets on a straight-line basis. Fixed asset purchases greater than \$1,000 are capitalized, with purchases below that threshold expensed as incurred.

Fair Value of Financial Instruments: The carrying values of operating funds, accounts receivable, payables and accrued expenses are considered to approximate the fair values of such at June 30, 2019 and 2018, due to the short-term maturity of these financial instruments. Committed loan support funds and other committed support funds are carried at fair value as further described in *Note I--Fair Value Measurements*.

Loans receivable are carried at face value, less loan loss reserves. Notes payable are carried at face value. Carolina Small Business makes and receives loans with stated interest rates that are consistent with community development market rates. Therefore, management believes the net carrying values of loans receivable and notes payable approximate the fair values of these financial instruments.

Functional Allocation of Expenses: The Organization allocates its expenses on a functional basis among its various programs and support services. Expenses that can be identified with a specific program and support service are allocated directly thereto. Certain indirect expenses are allocated to programs based on estimated usage and/or benefit.

Use of Estimates: The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of support, revenues and expenses during the reporting period. Actual results could differ from these estimates. Refer also to *Note D--Loans Receivable/Loan Loss Reserves* as pertains to a significant estimate.

Reclassifications: Certain amounts previously reported in the 2018 financial statements have been reclassified to conform to the 2019 presentation.

Carolina Small Business Development Fund

NOTE A--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -- Continued

Future Pronouncements: In June 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU are intended to assist entities (1) in evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal) transactions and (2) in determining whether a contribution is conditional. The standard will be effective for the resource recipient in fiscal years beginning after December 15, 2018, and for the resource provider in fiscal years beginning after December 15, 2019. Management is currently evaluating the impact of the adoption of this ASU on future financial statements.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. The ASU requires that amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period amounts shown on the statement of cash flows. The standard will be effective for fiscal years beginning after December 15, 2018. The ASU should be applied using a retrospective transition method to each period presented. Management is currently evaluating the impact of the adoption of this ASU on future financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The update introduced the expected credit losses methodology for the measurement of credit losses on financial assets measured at amortized cost basis, replacing incurred loss methodology. The standard will be effective for fiscal years beginning after December 15, 2022. Management is currently evaluating the impact of the adoption of this ASU on future financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, *Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than twelve months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Organization is currently evaluating the impact of the adoption of this ASU on future financial statements.

NOTE B--AVAILABILITY AND LIQUIDITY OF ASSETS (including a subsequent event)

The following reflects the Organization’s financial assets that are available for general expenditures within one year of the statement of financial position date (June 30):

	<u>2019</u>	<u>2018</u>
General deposits	\$ 1,758,495	\$ 1,457,425
Operating deposits	415,643	1,607,104
Grants receivable	688,145	688,178
Other receivables	74,441	72,695
Less: Minimum cash balance required by lender	<u>(300,000)</u>	<u>(300,000)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 2,636,724</u>	<u>\$ 3,525,402</u>

At June 30, 2020, management is also negotiating to obtain a \$500,000 bank line of credit to be used for working capital.

Carolina Small Business Development Fund

NOTE C--SIGNIFICANT CONCENTRATIONS (including subsequent events)

Deposit Risk: Carolina Small Business maintains operating deposits and other support funds at various financial institutions, the financial condition and credit ratings of which are monitored by the Organization's management on an ongoing basis. Deposit accounts are eligible for up to \$250,000 of insurance coverage per bank (credit union) provided by the Federal Deposit Insurance Corporation (National Credit Union Administration). Deposits in excess of federally insured limits approximated \$8,559,000 at June 30, 2019, though the Organization has incurred no loss as a result of such.

Investment Risk: Bank and credit union holdings at June 30, 2019, include certificates of deposit and share term certificates maturing at various dates between July 2020 and November 2023, and bearing interest at rates ranging from 0.997% to 3.25%. The Organization took early withdrawals of approximately \$251,000, \$494,000, and \$500,000 against these certificates in October 2019, December 2019, and May 2020, respectively. Proceeds from these early withdrawals provided the Organization with cash for operating expenses given the State's delayed, and still pending, approval of the 2019-2020 State Budget. The Organization paid penalties of approximately \$6,800 on the early withdrawals. Refer also to *Support Risk* below.

Credit Risk: At June 30, 2019, loans receivable includes outstanding balances from four borrowers of \$1,700,000, \$642,914, \$531,643, and \$393,045. None of these loans were past due at June 30, 2019, or subsequent thereto. At June 30, 2019, grants receivable includes \$518,702 due from a state agency under a disaster recovery loan program. At the date on which the financial statements were available to be issued, approximately \$369,000 of this receivable remains outstanding. The program was recently reassigned to a new state agency to administer. Management understands that grant payments were delayed due to this transition, but are expected to be forthcoming.

Support Risk: Carolina Small Business was appropriated \$2,500,000 by the North Carolina General Assembly to provide small business loans and financial training to start-ups and existing businesses and lending services to community-based organizations for each of the fiscal years ended June 30, 2019 and 2018. This appropriation represented approximately 28% and 36% of the Organization's total support and revenues for the years ended June 30, 2019 and 2018, respectively. At the date on which the financial statements were available to be issued, the 2019-2020 State Budget had not yet been approved. This one-year delay, and potential reduction or loss, in funding has had a significant impact on the Organization's operations. Management responded by reducing costs (related primarily to staffing), taking early withdrawals against certificates of deposit and share term certificates, obtaining more favorable repayment terms from lenders, and securing additional sources of support and revenue. Certain grantors also temporarily released restrictions on funds, making the support available for general operations pending receipt of State-appropriated funds. Refer also to *Note L--Commitments and Contingencies* as pertains to *Management's Evaluation of Going Concern*.

Carolina Small Business Development Fund

NOTE D--LOANS RECEIVABLE / LOAN LOSS RESERVES

Loans receivable of \$29,307,834 (including 425 loans) and \$30,209,030 (including 421 loans) at June 30, 2019 and 2018, respectively, are due from small businesses in underserved communities throughout North Carolina. Outstanding loans at June 30, 2019 have terms ranging from one to twenty years and bear interest at rates ranging from 0% to 11.5%. Refer also to *Note L--Commitments and Contingencies* as pertains to no-interest forgivable loans.

Principal maturities of loans receivable approximate the following at June 30, 2019:

<u>Years Ending June 30</u>	
2020	\$ 7,200,574
2021	4,039,669
2022	3,249,112
2023	4,383,598
2024	2,491,247
Thereafter	<u>7,943,634</u>
	<u>\$ 29,307,834</u>

Charge-Offs: Charge-offs of \$1,994,025 and \$549,140 were taken against loans receivable for the years ended June 30, 2019 and 2018, respectively. Loans are charged-off when all or a portion of the loan balance is deemed uncollectible.

Loan Loss Reserves: Loans receivable at June 30, 2019 and 2018, are recorded net of a provision for losses on loans of \$2,054,576 (7.0%) and \$2,404,592 (8.0%), respectively, based on management's estimates of inherent and probable credit losses. Management's estimates are based largely on assessed risk ratings and the significance of nonperforming, past due, and restructured loans.

At June 30, 2019, loans receivable of \$3,379,840 (11.53%) are due under nonperforming loans, including \$148,713 considered delinquent (90 days or more past due and still accruing) and \$3,231,127 in nonaccrual status. At June 30, 2018, loans receivable of \$2,534,970 (8.39%) are due under nonperforming loans, including \$649,541 considered delinquent (90 days or more past due and still accruing) and \$1,885,428 in nonaccrual status.

A loan is placed on non-accrual status when the loan approaches 90 days past due, when it becomes likely the borrower cannot or will not make scheduled principal or interest payments, when full repayment of principal and interest is not expected, foreclosure action is initiated, or when the loan evidences loss characteristics.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE D--LOANS RECEIVABLE / LOAN LOSS RESERVES--Continued

Other credit risk factors for the loan portfolio are summarized below:

<u>Risk Rating</u>	<u>Loan Balance</u>	<u>31 – 60 Days</u>	<u>61 – 89 Days</u>	<u>90 Days or More</u>	<u>Total Past Due</u>	<u>Troubled Debt Restructures</u>
<i>June 30, 2019</i>						
Pass	\$ 23,806,042	\$ 70,513	\$ 109,854	\$ 302,510	\$ 482,877	\$ 73,188
Watch	1,103,416	34,988	122,746	270,245	427,979	-
Classified	<u>4,398,376</u>	<u>96,627</u>	<u>186,977</u>	<u>2,286,164</u>	<u>2,569,768</u>	<u>1,458,342</u>
	<u>\$ 29,307,834</u>	<u>\$ 202,128</u>	<u>\$ 419,577</u>	<u>\$ 2,858,919</u>	<u>\$ 3,480,624</u>	<u>\$ 1,531,530</u>
<i>June 30, 2018</i>						
Pass	\$ 25,117,393	\$ 514,238	\$ 259,465	\$ -	\$ 773,703	\$ 97,534
Watch	219,223	-	-	-	-	-
Classified	<u>4,872,414</u>	<u>209,216</u>	<u>505,150</u>	<u>1,730,509</u>	<u>2,444,875</u>	<u>1,652,825</u>
	<u>\$ 30,209,030</u>	<u>\$ 723,454</u>	<u>\$ 764,615</u>	<u>\$ 1,730,509</u>	<u>\$ 3,218,578</u>	<u>\$ 1,750,359</u>

The general characteristics for each risk rating is as follows:

Pass—Loans meeting Carolina Small Business’s normal underwriting criteria, including loans with more than average credit risk. Business is able to sustain normal, temporary setbacks, but may not be strong enough to sustain major setbacks. Borrower may be highly or fully leveraged. Only one reliable repayment source may exist.

Watch—Loans not posing an immediate credit risk, but the borrower may have a deteriorated situation or setback that will likely improve. Recent trends in the borrower’s operations and/or financial situation warrant close attention. Loans require more than normal supervision and attention from the lender.

Classified—Loans having a high probability of payment default, or they have other well-defined weaknesses that put at risk the possibility of the debt being fully repaid or liquidated. Classified loans are generally characterized by current or projected operational losses, inadequate debt service coverage, insufficient liquidity, or limited capital. Unless the deficiencies are corrected or remedied, these loans will probably result in some loss. Loans assigned to this risk rating require extensive monitoring.

Significant Estimate: Carolina Small Business has recognized a provision for losses on loans at June 30, 2019 and 2018, based on management’s best estimate of uncollectible loans. Management believes that loan loss reserves adequately provide for potential losses; however, it is at least reasonably possible that management’s estimate of potential losses may change significantly in the near term.

Federal Loan/Loan Guarantee Programs: Carolina Small Business receives support and/or financing for small business lending under several federal programs. Lending activity under these programs is summarized as follows.

USDA–Intermediary Relending Program (IRP). Loans receivable of \$1,575,415 at June 30, 2019, bear interest at rates ranging from 5% to 8.75%, and are recorded net of a funded reserve for losses of \$120,691 (7.7% of outstanding loans). The program requires the Organization to maintain funded reserves of at least 6.0% of outstanding loans. Charge-offs of \$245,490 and \$52,849 were made during the years ended June 30, 2019 and 2018, respectively. Loans receivable of \$453,261 have payments over 60 days past due at June 30, 2019. Refer to *Note E--Notes Payable* as pertains to pay-back of the loan funds.

Carolina Small Business Development Fund

NOTE D--LOANS RECEIVABLE / LOAN LOSS RESERVES--Continued

USDA--Rural Micro-entrepreneur Assistance Program (RMAP). Loans receivable of \$459,718 at June 30, 2019, bear interest at rates ranging from 7% to 10.25%, and are recorded net of a funded reserve for losses of \$61,269 (13.3% of outstanding loans). The program requires the Organization to maintain funded reserves of at least 5.0% of outstanding loans. Charge-offs of \$112,108 and \$46,993 were made during the years ended June 30, 2019 and 2018, respectively. Loans receivable of \$44,149 have payments over 60 days past due at June 30, 2019. Refer also to *Note E--Notes Payable* as pertains to pay-back of the loan funds.

SBA Intermediary Lending Pilot (ILP) Program. Loans receivable of \$543,024 at June 30, 2019, bear interest at rates ranging from 5% to 8.5%, and are recorded net of a funded reserve for losses of \$50,173 (9.2% of outstanding loans). The program requires the Organization to maintain funded reserves of at least 5.0% of outstanding loans. Charge-offs of \$105,919 and \$0 were made for the years ended June 30, 2019 and 2018, respectively. Loans receivable of \$77,872 have payments over 60 days past due at June 30, 2019. Refer also to *Note E--Notes Payable* as pertains to pay-back of the loan funds.

Guaranteed Loan Programs. Carolina Small Business participates in certain guaranteed loan programs in order to provide long-term financing to small business concerns that would otherwise not be available

SBA Community Advantage Pilot Loan Program (CA) is a pilot loan program introduced by the U.S. Small Business Administration (SBA) to meet the credit, management, and technical assistance needs of small businesses in underserved markets. CA provides mission-oriented lenders access to 7(a) loan guaranties up to 85% for loans of \$250,000 or less. Approximately \$8,307,111 of the Organization's loans receivable at June 30, 2019, are guaranteed up to 75% or 85% by the CA program. The CA program requires the Organization to fund reserves of at least 5% of the unguaranteed portion of the CA loan portfolio, which approximates \$120,568 at June 30, 2019.

CA-guaranteed loans of \$2,543,386 were sold at a premium of \$96,561 in the secondary market during the year ended June 30, 2019. No such sales occurred during the year ended June 30, 2018. The Organization is required to fund reserves of at least 3% of the guarantee on loans sold which approximates \$105,462. Carolina Small Business held \$285,289 in a PNC-funded loan loss account at June 30, 2019, satisfying both the 5% (in preceding paragraph) and 3% reserve requirements. Refer also to *Note M--Subsequent Events*.

Charlotte Community Capital Fund Program (CCCF) is a program to provide financing to small businesses within the Charlotte, North Carolina region that show promise, but do not meet one or more of participating lenders' normal underwriting criteria. CCCF provides participating lenders access to loan guaranties up to 85% for loans of \$150,000 or less. Approximately \$408,324 of the Organization's loans receivable at June 30, 2019, are guaranteed up to 85% by the Charlotte Community Capital Fund.

North Carolina Capital Access Program (NC CAP) is a program run by NC Rural Center, and available to partner lenders in all 100 North Carolina counties. Under the NC CAP program, the borrower and the lender contribute a total of two to seven percent of the loan amount, and the NC Rural Center matches this amount dollar-for-dollar. These funds grow to create a reserve account that each participating lender may use to offset losses on enrolled loans, thus helping offset the lender's risk. At June 30, 2019, the NC CAP program holds approximately \$211,410 as a credit enhancement reserve for Carolina Small Business loans enrolled in the program. Enrolled loans have outstanding balances of approximately \$2,723,939 in the aggregate at June 30, 2019.

Loan Programs Added Subsequently: In September 2019, the Organization entered into a 5-year contract with Mecklenburg County to provide lending services to small businesses in Mecklenburg County. The contract is effective June 1, 2019, and includes an option to renew for one 3-year term. The County has committed to provide loan capital of \$2,750,000 for the program. CSBDF will receive management fees not-to-exceed \$500,000, plus servicing fees. Management fees are payable in quarterly payments of \$25,000 over the term of the contract.

Carolina Small Business Development Fund

NOTE D--LOANS RECEIVABLE / LOAN LOSS RESERVES--Continued

Loan Programs Added Subsequently--Continued: In March 2020, the Organization entered into a contract with the Rural Economic Development Center (Rural Center), whereby the Organization agrees to act as servicing agent for the Rural Center as pertains to loans made under the NC Rapid Recovery Loan Program. CSBDF will retain interest from borrowers and a portion of application and origination fees.

In April 2020, the Organization entered into a 10-year contract to provide lending services to small businesses located in Mecklenburg County. The County has committed to provide loan capital of \$5,000,000 for this Emergency Stabilization Loan Fund. CSBDF will receive management fees not-to-exceed \$1,000,000, plus servicing fees. Management fees of \$500,000 were received in April 2020, with \$500,000 payable ratably over the 10-year term.

In May 2020, the Organization entered into a contract with the City of Raleigh for the establishment of the Raleigh Small Business COVID-19 Relief Fund. CSBDF will be responsible for administering the program, including seeking contributions to support the efforts of the Fund. The City of Raleigh has committed loan capital of \$855,400. CSBDF will receive an administrative fee of \$84,600, plus transactional fees as defined by the contract.

On June 11, 2020, the Organization entered into a contract with the City of Durham whereby the Organization agrees to administer and seek contributions for the Durham Small Business Recovery Fund. Loan capital of \$2,000,000 from public and private sources will be used to establish the Fund, which will make loans and grants to preserve small businesses within the City of Durham that have been impacted by the COVID-19 pandemic. CSBDF will be paid administrative fees of \$200,000 within 30 days of contract execution, technical assistance fees of \$100,000 payable in two equal payments on July 15, 2020 and July 15, 2021, plus certain servicing and transactional fees as defined by the contract.

On June 22, 2020, Durham County voted to add \$1,000,000 to the City of Durham Small Business Recovery Fund. Durham County will pay CSBDF \$83,333 for loan administration within 30 days of contract execution, as well as \$83,333 over the course of fiscal 2021 and 2022 for technical assistance.

Refer also to *Note L--Commitments and Contingencies* as pertains to COVID-19 relief funding programs.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE E--NOTES PAYABLE (including subsequent events)

Notes payable consist of the following:

Creditor	Principal Payments	Interest Rate	Interest Payments	Maturity Date	Collateral	Principal Balance	
						June 30, 2019	June 30, 2018
First Bank	Due in full at maturity	2.00%	Monthly	Dec. 2020	Unsecured	\$ 250,000	\$ 250,000
Mercy Investment Services	Due in full at maturity, as extended	3.50%	Quarterly	May 2024	Unsecured	500,000	500,000
Capital Bank (formerly Community One Bank)	Monthly beginning February 2019, as amended	3.25%	Monthly beginning Feb. 2019	Dec. 2019	Unsecured	541,860	1,000,000
First Horizon Bank (formerly Capital Bank)	Monthly beginning October 2019, deferred for Apr, May, Jun 2020*	3.50%	Monthly beginning Oct. 2019*	Dec. 2020*	Unsecured	1,000,000	1,000,000
TD Bank	Paid in full at maturity	3.35%	Monthly	July 2018	Unsecured	0	500,000
TD Bank	Quarterly beginning June 2019, as amended	5.00%	Monthly	Mar. 2023	Unsecured	497,772	500,000
Woodforest National Bank	\$500,000 due Oct. 2020 and June 2021**	2.50%	Monthly	June 2021	Unsecured	1,000,000	1,000,000
Woodforest National Bank	Due in full at maturity	3.00%	Monthly	Dec. 2027	Unsecured	525,000	525,000
Appalachian Community Capital	Due in full at maturity	3.48% (Cost of Funds + 1%)	Monthly	Oct. 2021	Unsecured	1,000,000	1,000,000
Appalachian Community Capital	Due in full at maturity	2.00%	Monthly	Dec. 2022	Unsecured	100,000	100,000
USDA RMAP	Monthly	2.00%	Monthly	Aug. 2034	Partially secured by RMRF deposits/loans receivable	450,439	476,084
USDA RMAP	Monthly beginning May 2019	2.00%	Monthly beginning May 2019	April 2037	Partially secured by RMRF deposits/loans receivable	481,810	475,000
Bank of North Carolina	Due in full at maturity	3.00%	Quarterly	Feb. 2022	Partially secured by loans receivable	1,250,000	1,250,000
First National Bank	Due in full at maturity	3.00%	Monthly	Oct. 2022	Unsecured	1,100,000	1,100,000
Annie Casey Foundation	Due in full at maturity	3.00%	Quarterly	Dec. 2022	Unsecured	2,000,000	2,000,000
US SBA ILP	Quarterly	1.00%	Quarterly	Sep. 2031	Partially secured by ILP deposits/loans receivable	708,874	763,228
CNote Group, Inc.	Due in full at maturity	3.60% (variable)	Monthly	Aug. 2020	Unsecured	116,000	116,000
First Tennessee	Due in full at maturity	2.75%	Quarterly	Jan. 2028	Unsecured	500,000	500,000
Wells Fargo	Quarterly beginning April 2026	2.00%	Quarterly	Apr. 2028	Unsecured	1,000,000	1,000,000
Wells Fargo	Quarterly beginning May 2024	2.00%	Quarterly	May 2026	Unsecured	500,000	500,000
Bank of America	Annually beginning December 2020	3.25%	Quarterly	Dec. 2022	Partially secured by Borrower's title and interest in End Loans	1,000,000	1,000,000

*as amended subsequently.

**as modified subsequently, based on lender's expressed intent.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE E--NOTES PAYABLE (including subsequent events)--Continued

Creditor	Principal Payments	Interest Rate	Interest Payments	Maturity Date	Collateral	Principal Balance	
						June 30, 2019	June 30, 2018
Bank of America	Annually beginning August 2024	1.00%	Quarterly	Aug. 2026	Unsecured	525,000	0
Goldman Sachs	Quarterly beginning January 2018	4.50%	Monthly	Dec. 2022	Partially secured by GS deposits/loans receivable	1,837,151	2,467,619
Opportunity Finance Network	Quarterly beginning December 2019, \$450,000 balloon at maturity**	3.75%	Quarterly	Sep. 2021**	Partially secured by loans receivable	500,000	500,000
Opportunity Finance Network	Quarterly beginning December 2019, \$450,000 balloon at maturity**	3.75%	Quarterly	Sep. 2021**	Partially secured by loans receivable	495,640	500,000
PNC Bank	Rolled into new consolidated note, October 2018	4.00%	Quarterly	Apr. 2021	Unsecured	0	500,000
PNC Bank--LOC	Due in full at maturity	3.00%	Quarterly	Apr. 2021	Unsecured	1,000,000	1,000,000
PNC Bank--LOC	Rolled into new consolidated note, October 2018	4.00%	Quarterly	Apr. 2021	Partially secured by \$300,000 minimum deposit account	0	1,500,000
PNC Bank - new consolidated note	Quarterly beginning January 2019, \$1,456,000 balloon at maturity	4.00%	Quarterly	Apr. 2021	Partially secured by \$300,000 minimum deposit account	1,876,125	0
USDA IRP	Annually	1.00%	Annually	Nov. 2040	Partially secured by IRP deposits/loans receivable	626,134	651,460
USDA IRP	Annually	1.00%	Annually	May 2030	Partially secured by IRP deposits/loans receivable	221,637	240,614
USDA IRP	Annually beginning September 2019	1.00%	Annually	Sep. 2036	Partially secured by IRP deposits/loans receivable	625,000	625,000
USDA IRP	Annually	1.00%	Annually	Jan. 2046	Partially secured by IRP deposits/loans receivable	304,799	315,487
NMTC-PNC	Due in full at maturity	3.50%	Quarterly	Oct. 2025	Secured by QALICB loans receivable and underlying collateral	2,135,000	0
NMTC-PNC	Due in full at maturity	3.50%	Quarterly	Oct. 2025	Secured by QALICB loans receivable and underlying collateral	915,000	0
Total Notes Payable						\$ 25,583,241	\$ 23,855,492

*as amended subsequently.

**as modified subsequently, based on lender's expressed intent.

QALICB=Qualified Active Low-income Community Business

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE E--NOTES PAYABLE (including subsequent events) -- Continued

Interest expense totaled \$782,340 and \$594,090 for the years ended June 30, 2019 and 2018, respectively.

Principal maturities of notes payable at June 30, 2019 approximate the following, after giving effect to the subsequent modifications noted by an asterisk (*) on the previous two pages:

<u>Years Ending June 30</u>	
2020	\$ 2,122,156
2021	5,609,860
2022	4,214,657
2023	4,388,856
2024	701,163
Thereafter	<u>8,546,549</u>
	<u>\$ 25,583,241</u>

Available to Borrow for Small Business Lending: At June 30, 2019, loan funds of \$1,000,000 provided under the USDA Intermediary Relending Program are available to be drawn through September 30, 2021, for small business lending in Bladen, Columbus, and Robeson counties. Any amounts drawn hereunder will be subject to interest-only payments at 1.0% for the first 3 years, per the note agreement, with principal and interest payments required for the remaining 27 years of the note term.

Subsequent Events: Effective July 5, 2019, the Organization entered into a note agreement with CNote Group, Inc., whereby the lender agrees to extend loans of up to \$1,000,000, in the aggregate, with proceeds to be used to provide lending and financial assistance to women-led enterprises. Each note will require quarterly interest payments (at 4.5%), with principal due five years from the date of issuance.

On July 8, 2019, the Organization also closed on a \$300,000 note with C-Note/Wisdom Fund, requiring quarterly payments of interest at 4.5%, with outstanding principal due upon maturity in July 2024.

On May 4, 2020, the Organization was approved for a Paycheck Protection Program *forgivable* loan of \$656,900. Refer also to *Note L--Commitments and Contingencies* as pertains to COVID-19.

At June 30, 2020, management is negotiating to obtain a \$500,000 bank line of credit to be used for working capital. The line is expected to require monthly interest-only payments, with principal due upon maturity (in approximately one year).

Financial Covenants/Ratios: Certain of the preceding notes payable require the Organization to comply with various financial covenants and ratios over the terms of the related notes. The Organization met these commitments at June 30, 2019 and subsequent thereto, or has obtained waivers or acknowledgements from lenders accepting such.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE F--NET ASSETS WITH DONOR RESTRICTIONS / CONDITIONAL AWARDS (including subsequent events)

Net assets with donor restrictions were released from restrictions upon satisfaction of donor-imposed purpose and/or time restrictions as follows:

	Years Ended June 30,	
	<u>2019</u>	<u>2018</u>
Small business lending	\$ 627,954	\$ 629,408
Women's Business Center	260,899	298,826
Business services programming	51,548	-
Training and technical assistance	278,234	131,118
NC Disaster Recovery Loan Program	136,970	1,009,314
General operations	<u>71,965</u>	<u>123,468</u>
	<u>\$ 1,427,570</u>	<u>\$ 2,192,134</u>

Net assets with donor restrictions are available for the following purposes at June 30:

	<u>2019</u>	<u>2018</u>
Small business lending	\$ 1,698,930	\$ 898,138
Training and technical assistance	367,076	363,434
NC Disaster Recovery Loan Program	2,594,760	1,365,329
Business services programming	48,453	-
General operations	<u>-</u>	<u>13,500</u>
	<u>\$ 4,709,219</u>	<u>\$ 2,640,401</u>

Support from awards for the following remains conditional at June 30, 2019:

Small business lending	\$ 6,210,024
Women's Business Center	24,653
Training and technical assistance	277,560
NC Disaster Recovery Loan Program	<u>2,231,298</u>
	<u>\$ 8,743,535</u>

No amounts pertaining to conditional awards are included in the accompanying financial statements.

Subsequent Events: In December 2019, a donor removed conditions on an award of \$402,000 for small business lending and reclassified the grant funds for operating support. A payment of \$201,000 was received in December 2019, with a final payment of \$201,000 scheduled for funding in September 2020.

NOTE G--OPERATING LEASES (including subsequent events)

The Organization leases its primary office space in Raleigh under an operating lease scheduled to expire in October 2020. The lease requires minimum rentals plus pro rata payments for common area maintenance. The lease, as subsequently amended in April 2020, expires in April 2028 and provides for the conditional abatement of rent from May 2020 to October 2020. The lease may be extended for one five-year period with base rent at fair market value.

The Organization also leases office space for its Innovation and Entrepreneurship Center in Raleigh, for its Western Women's Business Center in Asheville, and for a satellite office in Charlotte. The Innovation and Entrepreneurship Center lease expired on December 31, 2019, and was not renewed.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE G--OPERATING LEASES (including subsequent events)--Continued

Rent expense under these operating leases approximated \$210,090 and \$204,723 for the years ended June 30, 2019 and 2018, respectively.

Future minimum rentals for leases having an initial term of one year or more, including effects of subsequent renewals, are as follows:

<u>Years Ending June 30</u>	
2020	\$ 154,041
2021	101,279
2022	148,640
2023	153,076
2024	157,656
Thereafter	<u>678,453</u>
	<u>\$ 1,393,145</u>

NOTE H--EMPLOYEE BENEFIT PLAN

Carolina Small Business sponsors a 401(k) retirement plan. Employees are eligible to participate after attaining age 21 and completing one month of service. The Organization makes Safe Harbor matching contributions at the rate of 100% of a participant's elective deferrals up to 5% of the participant's Compensation for the plan year. Employer matching contributions totaled \$100,094 and \$97,451 for the years ended June 30, 2019 and 2018, respectively. The plan also provides for discretionary, nonelective employer contributions, though no such contributions were approved for the years ended June 30, 2019 and 2018.

NOTE I--FAIR VALUE MEASUREMENTS

Carolina Small Business applies U.S. generally accepted accounting principles (GAAP) for fair value measurements of financial assets that are recognized or disclosed at fair value in the financial statements on a recurring basis. GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP also establishes a framework for measuring fair value and expands disclosures about fair value measurements.

FASB ASC 820-10 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value of financial instruments. This hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, Level 2 inputs consist of observable inputs other than quoted prices for identical assets, and Level 3 inputs have the lowest priority.

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE I--FAIR VALUE MEASUREMENTS--Continued

The following represents assets and liabilities measured (and carried) at fair value on a recurring basis by Carolina Small Business:

<u>June 30, 2019</u>	<u>Fair Value</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Operating funds	\$ 1,569,077	\$ -	\$ 1,569,077	\$ -
Committed loan support funds	2,861,722	2,861,722	-	-
Other committed support funds	258,596	-	160,200	98,396
Loans receivable	29,307,834	-	29,307,834	-
Notes payable	<u>25,583,241</u>	<u>-</u>	<u>25,583,241</u>	<u>-</u>
Total	<u>\$ 59,580,470</u>	<u>\$ 2,861,722</u>	<u>\$ 56,620,352</u>	<u>\$ 98,396</u>
<u>June 30, 2018</u>	<u>Fair Value</u>	<u>(Level 1)</u>	<u>(Level 2)</u>	<u>(Level 3)</u>
Operating funds	\$ 1,315,900	\$ -	\$ 1,315,900	\$ -
Committed loan support funds	1,364,939	1,364,939	-	-
Other committed support funds	273,821	-	171,262	102,559
Loans receivable	30,209,030	-	30,209,030	-
Notes payable	<u>23,855,492</u>	<u>-</u>	<u>23,855,492</u>	<u>-</u>
Total	<u>\$ 57,019,182</u>	<u>\$ 1,364,939</u>	<u>\$ 55,551,684</u>	<u>\$ 102,559</u>

Level 1: Committed loan support funds include holdings in money market and money market share accounts, the carrying value of which approximates the fair value.

Level 2: Operating funds and other committed support funds include holdings in share term certificates and certificates of deposit, the carrying values of which approximate the fair values based on current market rates for financial instruments of similar size and remaining maturities. Certificates held at June 30, 2019, mature at various dates from July 2020 to November 2023 and bear interest at rates ranging from 0.997% to 3.25%. Certificates held at June 30, 2018, mature at various dates from July 2018 to November 2022 and bear interest at rates ranging from 1.05% to 3.0%. The carrying value of loans receivable and notes payable approximate the fair values of such based on community development market rates for financial instruments with similar terms and remaining maturities.

Level 3: Other committed support funds include mortgages purchased from GCCU, the fair value of which approximates principal due from borrowers, less a loan loss reserve. Given the delinquent status of these loans when purchased from GCCU and the lack of comparable market data for properties similar to those securing these mortgages, management considers the fair value of these outstanding mortgages to be based on Level 3 inputs.

Fair Value Measurements Using Significant Unobservable Inputs (Level 3):

	Year Ended	
	<u>June 30, 2019</u>	<u>June 30, 2018</u>
Beginning balance, beginning of year	\$ 102,559	\$ 105,894
Collections on mortgages purchased from GCCU	<u>(4,163)</u>	<u>(3,335)</u>
Ending balance, end of year	<u>\$ 98,396</u>	<u>\$ 102,559</u>

Notes to Financial Statements--Continued

Carolina Small Business Development Fund

NOTE I--FAIR VALUE MEASUREMENTS -- Continued

The Organization reports transfers between levels of the fair value hierarchy, if any, at the end of the reporting period. There were no such transfers at June 30, 2019 and 2018.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while Carolina Small Business believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a significantly different fair value measurement at the reporting date.

NOTE J--TAX STATUS

Carolina Small Business Development Fund is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (IRC) and applicable state law, except on net income, if any, derived from unrelated business activities. The Organization believes that it has appropriate support for any tax positions taken, and as such, does not have any uncertain tax positions that are material to the financial statements. The Organization qualifies for the charitable contributions deduction under Section 170(b)(1)(A)(vi) and, therefore, has been qualified as an organization that is not a private foundation under Section 509(a)(2).

NOTE K--RELATED PARTY TRANSACTION

In July 2018, the Organization extended a loan of \$1,700,000 to EMP Commercial, LLC, owned by Eagle Market Streets Development Corporation (a CDC/Eagle Market Streets, hereafter) and Mountain Housing Opportunities, Inc. (Mountain Housing). The loan requires 87 monthly interest-only payments (at approximately 3.50%), with principal due in full on October 31, 2025. All loan documents, including unlimited guarantees on the loan, were signed by both Eagle Market Streets and Mountain Housing. The signer on behalf of Eagle Market Streets was its President/Manager, who also serves as the Vice Chair for CSBDF's Board of Directors. The Vice Chair abstained from voting when the Board approved the loan to EMP Commercial, LLC.

NOTE L--COMMITMENTS AND CONTINGENCIES (including subsequent events)

The Organization has committed to repay one-half of principal collected on certain disaster recovery loans. At June 30, 2019, loans receivable of \$964,742 are subject to this repayment provision. Principal maturities are scheduled as follows at June 30, 2019: \$100,513 in fiscal 2020; \$134,346 in fiscal 2021; \$95,246 in fiscal 2022; \$87,629 in fiscal 2023; \$69,313 in fiscal 2024; and \$477,695 thereafter.

The Organization participates in a forgivable disaster loan program whereby one-third of no-interest loan principal is forgiven at the end of years one, two, and three if certain requirements are met. If not forgiven, repayment of these loans is due in full as defined by agreement within the three-year term. Loans totaling \$100,000 were forgiven in fiscal 2019. Loans of \$1,450,000 remain outstanding at June 30, 2019.

Financial assistance from various awarding agencies is subject to special audit. Such audits could result in claims against Carolina Small Business for disallowed costs or noncompliance with grantor restrictions. Management is aware of no disallowable costs or other instances of noncompliance with grantor restrictions that may have a direct and material effect on the accompanying financial statements. Consequently, no provision has been made for liabilities, if any, that may arise from special audits by grantor agencies.

Carolina Small Business Development Fund

NOTE L--COMMITMENTS AND CONTINGENCIES (including subsequent events) -- Continued

COVID-19: On March 11, 2020, the World Health Organization declared COVID-19 a global health pandemic. The State of North Carolina operated under a “Stay at Home” order from March 27, 2020 to May 8, 2020. CSBDF’s staff began working remotely in late-March, but continued to assist small businesses in need of emergency relief funding. The Organization’s COVID-19 relief programs include the following: (1) NC Rapid Recovery Loan Program, with loans available up to \$50,000 based on the business’s current revenues; (2) Mecklenburg County Small Business Emergency Stabilization Loan Fund to support small businesses in Mecklenburg County with loans from \$5,000 to \$35,000; (3) City of Raleigh Small Business COVID-19 Relief Fund with grants available up to \$10,000 or two months’ rent (whichever is less) for storefront firms with less than 50 employees; and (4) the Durham Small Business Recovery Fund, making grants to small businesses in Durham with annual revenues of \$500,000 or less and loans to small businesses with annual revenues greater than \$500,000 and up to \$2,000,000. All businesses receiving assistance must have been adversely impacted by COVID-19.

The Organization’s existing borrowers may also be eligible for certain loan deferrals or modifications during the COVID-19 pandemic. Payments are automatically deferred by the CARES Act (*Coronavirus Aid, Relief, and Economy Security Act*) for borrowers that have a loan guaranteed by the Small Business Administration.

In order to continue assisting small businesses during the pandemic, the Organization applied for, and was awarded, a *forgivable loan* under the Paycheck Protection Program (PPP), a program administered through the U.S. Small Business Administration and created with the enactment of the CARES Act. The Organization received loan proceeds of \$656,900 on May 14, 2020. Management expects the PPP loan to be eligible for forgiveness based on the Organization’s intent to use the proceeds therefrom to fund eligible payroll and other qualifying expenses within 24 weeks of receipt. Per program guidelines, any portion of a loan that is not eligible for forgiveness will bear interest at 1.0%, with payments of interest deferred until SBA determines the amount of the loan that will be forgiven and pays that amount to the lender. Thereafter, the note will require monthly payments of principal and interest over a two-year maturity period, unless the lender agrees to an extended maturity period. PPP loans are unsecured.

The Organization also received an SBA Economic Injury Disaster Loan (EIDL) of \$150,000 on June 16, 2020.

The State of North Carolina is scheduled to enter Phase Three of its re-opening plan as early as July 17, 2020. Social distancing and certain other restrictions are expected to be in place for much, if not all, of 2020. Management expects that CSBDF employees will continue working remotely until at least the fall of 2020. At the date the financial statements were available to be issued, management continues to monitor the situation; however, the impact of COVID-19 on the Organization’s operations cannot be reasonably estimated at this time.

Management’s Evaluation of Going Concern: As indicated in the financial statements, the Organization reported deficit changes in net assets without donor restrictions of (\$1,252,855) and (\$254,810) for the years ended June 30, 2019 and 2018, respectively. The deficit change in net assets without donor restrictions for fiscal 2019 is largely due to an increase in the provision for losses on loans.

The Organization received a State appropriation of \$2,500,000 for each of the years ended June 30, 2019 and 2018. These appropriations represented approximately 28% (2019) and 36% (2018) of the Organization’s total support and revenues in those fiscal years. At the date on which the financial statements were available to be issued, the NC State Budget for fiscal 2019-2020 has not yet been approved. The State of North Carolina is facing significant budget shortfalls as a result of the COVID-19 pandemic. Although the State is expected to pass budgets for fiscal 2019-2020 and fiscal 2020-2021 in the near term, it is not yet known whether the Organization will receive a State appropriation for either fiscal 2020 or fiscal 2021.

These factors create uncertainty as to whether the Organization will be able to meet its obligations when due within twelve months from the date on which the financial statements were available to be issued. Management has considered these factors and has taken the following steps to address these concerns.

Carolina Small Business Development Fund

NOTE L--COMMITMENTS AND CONTINGENCIES (including subsequent events) -- Continued

Management's Evaluation of Going Concern--Continued: Management eliminated all non-essential costs from the Organization's operating budget for fiscal 2020 and is committed to doing so for fiscal 2021 and beyond. Cost reductions include a conditional abatement of rent for May 2020 to October 2020, negotiated upon extension of the Organization's primary office lease. Management also identified and secured additional sources of support for general operations. A grantor agreed in February 2020 to allow the Organization to repurpose \$760,000 of small business lending funds for general operations, pending receipt of a State appropriation; a grantor agreed in May 2020, to release lending conditions on support of \$402,000; PPP *forgivable* loan funds of \$656,900 and EIDL loan funds of \$150,000 were obtained in May 2020 and June 2020, respectively; and grants of approximately \$475,000 were awarded to the Organization subsequently for general expenditures.

The Organization has also played a vital role in making emergency relief loans to small businesses impacted by COVID-19. Contracts with local municipalities and state-funded agencies subsequently generated fees in excess of \$800,000. Loan administration for governmental units is expected to provide a significant source of revenue in fiscal 2021 and beyond.

Certain of the Organization's lenders subsequently agreed to extensions of loan maturities and/or deferrals of principal payments, as described in *Note E--Notes Payable*. At June 30, 2020, management is negotiating to obtain a \$500,000 bank line of credit and also expects to obtain additional extensions on notes maturing in the latter half of fiscal 2021.

Management believes these actions will enable the Organization to meet its obligations when due within twelve months from June 30, 2020, the date on which the financial statements were available to be issued.

NOTE M--SUBSEQUENT EVENTS (not otherwise disclosed herein)

Management has evaluated subsequent events through June 30, 2020, the date on which financial statements were available to be issued. All subsequent events for which U.S. GAAP requires adjustment or disclosure have been adjusted or disclosed.

SUPPLEMENTARY INFORMATION

Schedule of Federal and State Awards

Carolina Small Business Development Fund

Year Ended June 30, 2019

Grantor/ Pass-through Grantor/ Program Title	CFDA #	Pass-through Entity Identifying Number	Federal Expenditures	State Awards	
				Support	Expenditures
FEDERAL AWARDS:					
<u>U.S. Department of Agriculture, Rural Development:</u>					
<i>Rural Business Development Grant (RBDG):</i>					
Training and technical assistance to micro-borrowers	10.351		\$ 13,704		
<i>Intermediary Relending Program (IRP):</i>					
Loans due to federal agency at beginning of fiscal year	10.767		1,832,561		
<i>Rural Microentrepreneur Assistance Program (RMAP):</i>					
Training and technical assistance to micro-borrowers			14,757		
Loans due to federal agency at beginning of fiscal year	10.870		951,084		
			<u>965,841</u>		
<u>U.S. Department of Commerce, Economic Development</u>					
<u>Administration (EDA):</u>					
<i>Economic Adjustment Assistance Program:</i>					
Small business lending	11.307		25,000		
<u>U.S. Department of Housing and Urban Development:</u>					
<i>CDBG--Entitlement Grants Cluster/Community Development</i>					
<i>Block Grant Program for Entitlement Communities:</i>					
<u>City of Asheville, North Carolina:</u>					
<i>Opportunity Asheville: WWBC - Business Training and Access to Capital in the City of Asheville</i>	14.218	FY 2018-19	57,660		
<i>Community Development Block Grants/State's Program and Non-Entitlement Grants in Hawaii:</i>					
<u>North Carolina Department of Commerce:</u>					
<i>CDBG Business Recovery Assistance Program:</i>					
Small business lending			1,150,000		
Program expenses	14.228	CDBG-DR 17-R-3002	202,279		
			<u>1,352,279</u>		
<u>U.S. Small Business Administration:</u>					
<i>Women's Business Ownership Assistance:</i>					
SBAHQ-16-W-0005/0002			27,892		
SBAHQ-16-W-0005/0004	59.043		125,347		
			<u>153,239</u>		
<i>Prime Technical Assistance</i>	59.050		22,590		
<i>Intermediary Loan Program (ILP):</i>					
Loans due to federal agency at beginning of fiscal year	59.062		763,228		
			<u>763,228</u>		
TOTAL FEDERAL EXPENDITURES			\$ <u>5,186,102</u>		
STATE AWARDS:					
<u>State of North Carolina Special Appropriation of</u>					
<u>State General Fund:</u>					
North Carolina Department of Commerce:					
Small business lending (including committed funds)			\$ 300,000	\$ 300,000	
Loan loss reserves (committed)			100,000	100,000	
General operations			2,100,000	2,100,000	
		NC Grant ID 27898	<u>2,500,000</u>	<u>2,500,000</u>	
<u>State of North Carolina Appropriation under The Disaster</u>					
<u>Recovery Act of 2016:</u>					
The Golden Leaf Foundation:					
<i>North Carolina Disaster Recovery Loan Program:</i>					
Small business lending (loans placed)			-	168,232	
Program expenses			-	44,276	
		FY2017-149	<u>-</u>	<u>212,508</u>	
TOTAL STATE AWARDS			\$ <u>2,500,000</u>	\$ <u>2,712,508</u>	

See independent auditors' report as pertains to supplementary information and notes to schedule of federal and state awards.

Notes to Schedule of Federal and State Awards

Carolina Small Business Development Fund

Year Ended June 30, 2019

NOTE A--BASIS OF PRESENTATION

The accompanying schedule of federal and state awards (the Schedule) includes the federal and state grant activity of Carolina Small Business Development Fund for the year ended June 30, 2019. The information in the Schedule is presented in accordance with the requirements of Title 2 *U.S. Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Organization, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Organization.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following, as applicable, either the cost principles contained in Office of Management and Budget Circular A-122, *Cost Principles for Non-Profit Organizations*, or the cost principles contained in Title 2 *U.S. Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

NOTE C--FEDERAL LOAN / LOAN GUARANTEE PROGRAMS

The following federal loan programs are administered by the Organization, with balances and transactions relating to these programs included in the Organization's basic financial statements. Loans outstanding at the beginning of the fiscal year and loans taken during the fiscal year are included in the federal expenditures presented in the Schedule. The balance of loans due to the federal agencies at June 30, 2019 consists of:

<u>CFDA #</u>	<u>Program Name</u>	<u>Outstanding Balance June 30, 2019</u>
10.767	USDA IRP	\$ 1,777,569
10.870	USDA RMAP	932,249
59.062	US SBA ILP	708,874

Loans receivable from borrowers of approximately \$8,307,111 at June 30, 2019, are guaranteed (up to 75% or 85%) under the SBA Community Advantage Pilot Loan Program.

Loans receivable from borrowers of approximately \$429,935 at June 30, 2019, are guaranteed (up to 85%) under the Charlotte Community Capital Fund Program.

Loans receivable from borrowers of approximately \$2,723,939 at June 30, 2019, are guaranteed up to 7% under the NC Capital Access Program.

NOTE D--INDIRECT COST RATE

The Organization has elected not to use the 10% de minimis indirect cost rate allowed under the Uniform Guidance.

COMPLIANCE REPORTS



Independent Auditors' Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an
Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards*

Board of Directors
Carolina Small Business Development Fund
Raleigh, North Carolina

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Carolina Small Business Development Fund (a nonprofit organization), which comprise the statement of financial position as of June 30, 2019, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 30, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Carolina Small Business Development Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of Carolina Small Business Development Fund's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described in the accompanying schedule of findings and questioned costs, we did identify certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and questioned costs as item 2019-001 to be a material weakness.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of findings and questioned costs as item 2019-002 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Carolina Small Business Development Fund’s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Carolina Small Business Development Fund’s Response to Findings

Carolina Small Business Development Fund’s response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. Carolina Small Business Development Fund’s response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization’s internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the organization’s internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Romeo, Wiggins & Company, L.L.P.

Raleigh, North Carolina
June 30, 2020



Independent Auditors' Report on Compliance
for Each Major Program and on Internal Control
Over Compliance Required by the Uniform Guidance

Board of Directors
Carolina Small Business Development Fund
Raleigh, North Carolina

Report on Compliance for Each Major Federal Program

We have audited Carolina Small Business Development Fund's compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Organization's major federal programs for the year ended June 30, 2019. The Organization's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Carolina Small Business Development Fund's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 *U.S. Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Carolina Small Business Development Fund's compliance.

Opinion on Each Major Federal Program

In our opinion, Carolina Small Business Development Fund complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2019.

Report on Internal Control Over Compliance

Management of Carolina Small Business Development Fund is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Organization's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Carolina Small Business Development Fund's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Romeo, Wiggins & Company, L.L.P.

Raleigh, North Carolina
June 30, 2020

Schedule of Findings and Questioned Costs

Carolina Small Business Development Fund

Year Ended June 30, 2019

Section I - Summary of Auditors' Results

Type of auditors' report issued on financial statements: *Unmodified*

Internal control over financial reporting:

- ◆ Material weakness(es) identified? X yes no
- ◆ Significant deficiency (ies) identified? X yes none reported

Noncompliance material to financial statements noted? yes X no

Federal Awards

Internal control over major federal award programs:

- ◆ Material weakness(es) identified? yes X no
- ◆ Significant deficiency (ies) identified? yes X none reported

Noncompliance material to major federal award programs? yes X no

Type of auditors' report issued on compliance for major federal programs: *Unmodified*

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? yes X no

Identification of major federal programs:

<u>CFDA Number(s)</u>	<u>Program Name</u>
10.870	USDA Rural Microentrepreneur Assistance Program
14.228	HUD Community Development Block Grants/ State's Program and Non-Entitlement Grants in Hawaii

Dollar threshold used to distinguish between type A and type B programs: \$750,000

Auditee qualified as low-risk auditee? yes X no

Schedule of Findings and Questioned Costs--Continued

Carolina Small Business Development Fund

Year Ended June 30, 2019

Section II - Financial Statement Findings

Finding 2019-001: Loan File Maintenance and Servicing

Criteria: The Organization administers its small business lending program in accordance with Board-approved Loan Policies & Procedures. Funds for small business lending are provided by various federal and state agencies, financial institutions, and foundations, in the form of grants or loan funds. The Organization also participates in various credit enhancement programs, including the U.S. Small Business Administration's Community Advantage (SBA CA) program. Providers and guaranteeing entities may impose additional requirements on the placement and servicing of loans. To effectively administer its small business lending program, the Organization requires that a loan file be maintained for each loan. The file is required to include, among other things, an application package, completed credit memo or loan transmittal, pre-closing site visits, approvals for loans and loan modifications, executed loan and security agreements, updated financial information from borrowers, and documentation of collection efforts on past due loans.

Condition: We noted numerous instances in which loan files were missing updated financial information from the borrower. Often, the same loan files lacked documentation of approvals of the initial loan and/or loan modifications.

Context: We reviewed 39 loan files that were judgmentally selected from loans outstanding at June 30, 2019. Of these 39 loans, 14 are also SBA CA loans. We noted 17 instances (including 5 SBA CA loans) in which the files were missing updated financial information from borrowers. We also noted 10 instances (including 5 SBA CA loans) in which files were missing approvals for loans and/or loan modifications. We also noted one instance in which a pre-closing site visit was not performed for an SBA CA loan.

Cause: The Organization has a diverse loan portfolio with an average outstanding loan balance of approximately \$75,000 at June 30, 2019. Programs restricted for veterans and disaster relief victims were given additional emphasis in fiscal 2019 and required more extensive marketing and monitoring efforts. The Organization also experienced transitions in key personnel during fiscal 2019 that imposed inherent time constraints on the small business lending team.

Effect: The Organization failed to comply with its Loan Policies and Procedures for loan file maintenance and servicing as noted in *Condition* above.

Repeat Finding: This is considered a *repeat finding*.

Recommendation: We recommend the Organization re-emphasize the importance of maintaining loan files in accordance with its Loan Policies and Procedures, as well as with other requirements imposed by providers and guaranteeing entities. Roles and responsibilities for maintaining, monitoring, and servicing loan files should be clearly defined to ensure that files contain all required documentation and are updated on a timely basis. We also encourage management to consider whether staffing levels are appropriate given the increased size and complexity of the Organization's loan portfolio.

Views of responsible officials and planned corrective actions: Continued on the following page.

Carolina Small Business Development Fund

Section II - Financial Statement Findings--Continued

Finding 2019-001: Loan File Maintenance and Servicing--Continued

Views of responsible officials and planned corrective actions: We agree with the finding. Management continues to enhance procedure and practice in an ongoing effort to improve loan file maintenance and post-closing loan servicing. During FY 2019-2020 the Organization:

- Saw its Board of Directors take decisive steps to strengthen and support the Business Lending team.
- Hired two individuals with multiple years of commercial banking experience to serve in the roles of Portfolio Servicing Officer and Senior Loan Closer and to assist in the assembly and maintenance of the loan files.
- Has plans to hire a part-time Loan Support Specialist who will be directly involved with loan file review and periodic loan servicing tasks (first quarter FY 2020-2021).
- Introduced a new credit memorandum, revised loan file checklists, and loan approval practices that will prevent findings on new loan originations.
- Is currently implementing an automated loan approval process in Salesforce that will document the loan recommendation and loan approval within the software.
- Is currently implementing an organization-wide relationship management program, whereby Business Development Officers and Business Services Associates will become more involved in the servicing of the outstanding portfolio.

Finding 2019-002: Failure to Obtain Receipts for Credit Card Charges

Criteria: The Organization issues credit cards to management team members and the Fiscal Office with the approval of the President/CEO for approved CSBDF business transactions (including travel arrangements) or pre-authorized emergency purchases. Receipts for credit card charges, other than recurring charges, are required to be submitted to the Fiscal Office on a monthly basis. Receipts are required to be filed with the credit card statements.

Condition: We noted numerous charges on credit card statements for which no supporting receipts were available.

Context: We haphazardly selected 3 credit card statements which included all authorized cardholders for different months throughout fiscal 2019. Our sample included charges totaling \$86,979. Approximately \$5,530 (6%) of the charges tested, excluding recurring charges, lacked supporting receipts.

Cause: The Organization issued credit cards as a practical matter to designated employees. A significant amount of time was required to administer the program due to the late submission of receipts, as well as the number of cardholders (13 on average). Few, if any, consequences were imposed for late submissions or for failure to submit credit card receipts.

Effect: The Organization failed to obtain documentation to support the business nature and reasonableness of certain credit card charges.

Recommendation: We understand the Organization subsequently implemented SAP Concur, travel and expense management software. Employee business expenses and related receipts are now tracked and submitted electronically on a monthly basis. We commend management's efforts to facilitate expense reporting by employees, but we also encourage the Organization to more strictly enforce its credit card policies. Cardholders who continue to submit receipts on a delayed basis, or who fail to submit receipts, should be subject to the revocation of credit card privileges.

Views of responsible officials and planned corrective actions: Continued on the following page.

Schedule of Findings and Questioned Costs--Continued

Carolina Small Business Development Fund

Section II - Financial Statement Findings--Continued

Finding 2019-002: Failure to Obtain Receipts for Credit Card Charges--Continued

Views of responsible officials and planned corrective action: We agree with the finding. Management has implemented SAP Concur expense and invoicing software. All receipts are tracked and submitted electronically. The credit card expense report cannot be submitted until all receipts are attached. In response to the finding, the credit card policy was updated to require extra levels of authorization and stricter policies. If cardholders fail to comply with the Organization's policy, their credit card privileges will be subject to revocation.

Section III - Federal Award Findings and Questioned Costs

We have no such findings to report.



Summary Schedule of Prior Audit Findings

Current Audit Period: Year Ended June 30, 2019

Financial Statement Findings

Finding 2018-001: Recognition of Grant Support

Condition: The Organization recognized support from certain reimbursement grants prior to the incurrence of qualifying expenses.

Recommendation: We recommended that management re-emphasize the importance of maintaining the accounting records in accordance with GAAP on an ongoing basis to ensure the reliability and relevance of the Organization's in-house financial statements.

Current Status: The Organization subsequently adopted a policy, retroactive to July 1, 2018, requiring that reimbursement grants be monitored monthly by management to ensure that support is recognized only when the allowable expenses are incurred or related loans are placed. Monitoring was performed by management for all reimbursement grants in effect during fiscal 2018-2019, and adjustments were made as necessary to comply with generally accepted accounting principles. No similar findings were noted for fiscal 2019.

Finding 2018-002: Maintenance of Loan Files

Condition: Based on a review of 33 judgmentally-selected loan files, we noted numerous instances in which the files were missing updated financial information from the borrower. Management was generally able to provide a verbal update as to the borrower's current financial situation. We also noted several instances in which files were missing approvals for loans. Management was able to provide evidence of approvals in most of these cases. A few files lacked approvals for loan modifications and two loans were operating under modification agreements that expired during the first calendar quarter of 2018. We also noted two instances in which fees charged borrowers exceeded fees allowed by the grantor agency. In both instances, the Organization subsequently returned the excess fees to the borrowers.

Recommendation: We recommended the Organization re-emphasize the importance of maintaining loan files in accordance with its policies and procedures for such. We further encouraged management to redefine roles and responsibilities for updating and monitoring loan files to ensure the files are well-organized and contain all required documentation.

Current Status: Management recognizes the need to improve loan file maintenance and post-closing loan servicing. To address these needs the Organization has made key personnel hires during fiscal 2019-2020. These positions include a Portfolio Servicing Officer and a Senior Loan Closer. Both individuals have over 15 years of experience in commercial loan closing and SBA loan servicing. Based upon their experience, these associates will play major roles in helping to ensure that loan files contain all required documentation. Additionally, management continues to develop appropriate procedure and policy to encourage superior asset quality. As an example, management recently implemented a new credit memorandum and approval practice that ensures the appropriate loan approval is in the file prior to closing the loan.